

REPORT OF EXAMINATION  
OF THE  
ALLIANCE UNITED INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2004

Filed June 30, 2006

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Los Angeles, California  
April 7, 2006

Honorable John Garamendi  
Insurance Commissioner  
California Department of Insurance  
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

**ALLIANCE UNITED INSURANCE COMPANY**

(hereinafter also referred to as the Company) at its home office at 2125 Knoll Drive, Suite 100, Ventura, California 93003.

**SCOPE OF EXAMINATION**

The previous examination of the Company was made as of December 31, 2001. This examination covers the period from January 1, 2002 through December 31, 2004. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; accounts and records; and sales and advertising.

## SUBSEQUENT EVENTS

On December 23, 2005, a Form A was filed with the California Department of Insurance (CDI) for a change in control of the majority shareholder of the Company's parent, Alliance United Group (AUG). Mr. David Mandel and his wife, owners of Platinum Group of Companies, Inc. and the owners of 9.6% of the common stock of AUG, will purchase additional stocks of AUG valued at \$2.4 million. In addition, AUG will convert a \$300,000 note payable to the Mandels and \$400,000 in preferred stock of AUG held by the Mandels into common stock of AUG, which will increase the Mandels' ownership of the Company to 43%.

On December 21, 2005, the Mandels deposited \$750,000 into a trust account for the benefit of AUG with First California Bank of Camarillo, pending approval of the "Form A". On February 28, 2006, the \$750,000 was loaned by the Mandels to AUG and given to the Company as a surplus contribution from AUG.

## COMPANY HISTORY

The Company is a wholly-owned subsidiary of Alliance United Group (AUG), and was incorporated under the laws of the State of California on December 17, 1997, and commenced business on June 30, 1998.

Effective January 12, 2004, the California Department of Insurance (CDI) approved the acquisition of Thousand Anniversary Inc., formerly known as Carnegie Holding Inc., and its' subsidiary Alliance United Insurance Company, formerly known as Millennium Insurance Company, by Alliance United Group (AUG).

In connection with the acquisition of the Company by AUG, the CDI has restricted the Company from paying any dividends during the first three years of operation following the purchase of the Company from GuideOne Financial Group, Inc.

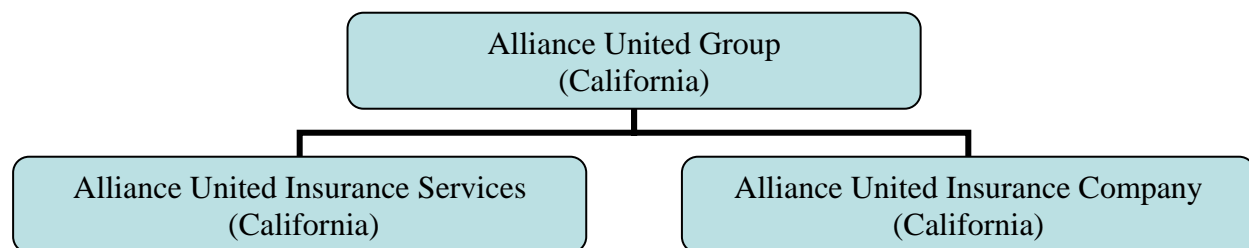
Effective September 2, 2004, the Company's name was changed from Millennium Insurance Company to Alliance United Insurance Company (AUIC).

During 2002, the Company received \$750,000 capital contribution from its parent.

During 2004, the Company received a capital contribution of \$1.5 million including a cash contribution of \$1,100,000 in March 2004 by Alliance United Group (AUG). Also, the Company recognized an account receivable of \$400,000 from AUG, which was paid to the Company in February 2005.

### MANAGEMENT AND CONTROL

The following is an organizational chart depicting the Company's relationship within the holding company system:



Management of the Company is vested in a seven-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2004 follows:

#### Directors

##### Names and Residence

Ted (NMN) Hume  
St. Louis, Missouri

##### Principal Business Affiliation

Chairman of the Board  
Alliance Insurance Group

#### Directors (cont.)

##### Names and Residence

##### Principal Business Affiliation

Brian J. Duffy  
Ventura, California

President, Chief Executive Officer and  
Assistant Secretary  
Alliance United Insurance Company

John F. Brandt  
Healdsburg, California

President  
The Brandt Insurance Agency

Bernard D. Bernacchi (\*)  
Oxnard, California

Partner  
Soares, Sandall, Benachchi and Petrovich, LLP

Lester M. Ireland  
Turlock, California

President and Chief Executive Officer  
Winton, Ireland, Storm & Green Insurance  
Agency

John E. Johnson  
San Leandro, California

President  
McDemott Costa Co. Inc. Insurance Agency

Phil E. VanSwoll  
Dublin, California

Senior Vice President  
CCI Financial Services

\* Resigned as of March 19, 2006.

#### Principal Officers

##### Names

##### Title

Brian J. Duffy

President, Chief Executive Officer  
and Assistant Secretary

Cory J. Mertes

Vice President, Chief Financial Officer and  
Secretary

Kjell P. Austad

Vice President Underwriting, Director of  
Marketing and Assistant Secretary

Brand B. Hinkle

Director of Claims

James B. Nicholson

Chief Technical Officer

## Management Agreements

**Tax Allocation Agreement:** the Company is party to a tax allocation agreement with Alliance United Group (AUG), and Alliance Insurance Services to prepare its federal income taxes on a consolidated basis, effective December 31, 2004. AUG will be responsible to calculate and file the consolidated federal income tax return and each company will compute its federal income tax liability or refunds on a separate basis and settle with its parent. The agreement was approved by the California Department of Insurance (CDI) on January 29, 2004.

**Administrative Services Agreement:** The Company and its affiliate, Alliance United Insurance Services (AUIS) entered into this agreement on January 1, 2004. Under the terms of the agreement, AUIS provides underwriting and administrative services, except claims handling services which are performed by the employees of the Company. The services provided by AUIS include, but are not limited to, financial reporting, tax return preparation and filing, administration and management of all bank and cash accounts, budget and cost accounting, human resource services, payroll services, legal services, office support, actuarial services, investment management, computer services, marketing and corporate affairs. The Company reimburses AUIS for the actual costs incurred. This agreement was approved by the CDI on January 29, 2004.

**Investment Management Agreement:** The Company is party to an agreement with Asset Allocation Management L.L.C. (AAM), effective January 15, 2004. According to the agreement, AAM manages the investments of the Company in accordance with investment objectives outlined in the agreement for a fee. This Agreement was approved by the CDI on January 29, 2004.

**Securities Custodial Agreement:** The Company entered into a securities custodial agreement with Wells Fargo Bank, N.A. on January 15, 2004. Wells Fargo Bank, N.A. is not a qualified custodian as defined in CIC Section 1104.9(a)(1). It is recommended that the Company execute an agreement with a qualified custodian and file the proposed agreement with the CDI in advance as required by CIC Section (1104.9(c).

General Agency Agreement: Effective January 1, 2004, the Company and AUIS entered into an agency agreement under which AUIS acts as a general agent for the Company. Under the terms of the agreement, AUIS will provide production, policy administration and servicing, including billing, collection of premiums, using rates and forms specified by the Company. AUIS may accept business from any sub-producer properly licensed. The Company will pay a maximum commission of 24%. This agreement was approved by the CDI on January 29, 2004.

General Agency Agreement: Effective December 31, 2004, the Company and Platinum General Insurance Agency, LLC (Platinum) entered into an Agency Agreement under which Platinum acts as a general agent for the Company. Under the terms of the agreement, Platinum may accept business through licensed sub-producers and receive a maximum commission of 21% from the Company. This agreement was submitted to the CDI for approval.

It is recommended that the Company amend its management agreements to reflect the name change of the Company from Millennium Insurance Company to Alliance United Insurance Company.

#### TERRITORY AND PLAN OF OPERATION

The Company is licensed only in California and is authorized to write fire, marine, disability, plate glass, liability, common carrier liability, boiler and machinery, burglary, sprinkler, team and vehicle, automobile, and miscellaneous. The Company offers the minimum financial responsibility limits of automobile liability with a \$2,000 medical payment limits, and up to \$40,000 physical damage limits. For the year 2004, the Company wrote \$5,604,975 in direct premiums which included \$3,571,101 in private passenger auto liability and \$2,033,874 of auto physical damage.

The Company markets its nonstandard private passenger automobile insurance through Alliance United Insurance Services, and Platinum General Insurance Agency, LLC and its affiliated producer, Low Cost Insurance Services, Inc.



The higher limit risks are placed with CSE Safeguard Insurance Company of San Francisco, California, under a general agency agreement with United Insurance Services.

### REINSURANCE

#### Assumed

The Company does not assume reinsurance.

#### Ceded

The Company has no reinsurance ceded on its current business. However, the Company has a reinsurance agreement with GuideOne Specialty Mutual Insurance Company, effective December 31, 2003. Under the terms of the agreement, the Company cedes 100% of the losses, loss adjustment expenses and IBNR related to the runoff business written on or before December 31, 2003.

### FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Underwriting and Investment Exhibit for the Year Ended December 31, 2004

Reconciliation of Surplus as Regards Policyholders  
from December 31, 2001 through December 31, 2004

Statement of Financial Condition  
as of December 31, 2004

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 7,398,287	\$	\$ 7,398,287	
Cash and short-term investments	1,084,006		1,084,006	(1)
Investment income due and accrued	70,990		70,990	
Uncollected Premiums and agents' balances in course of collection	2,220,584		2,220,584	
Net deferred tax asset	210,567	210,567		
Receivable from parent, subsidiaries and affiliates	<u>400,000</u>	<u></u>	<u>400,000</u>	
Total assets	<u>\$ 11,384,434</u>	<u>\$ 210,567</u>	<u>\$11,173,867</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 1,735,546	(2)
Loss adjustment expenses			309,000	(2)
Other expenses			83,611	
Taxes licenses and fees			128,645	(3)
Unearned premiums			2,276,257	
Payable to parent, subsidiaries and affiliates			<u>22,754</u>	
Total liabilities			4,555,813	
Common capital stock		\$ 2,600,000		
Gross paid-in and contributed surplus		6,650,000		
Unassigned funds (surplus)		<u>(2,631,946)</u>		
Surplus as regards policyholders			<u>6,618,054</u>	
Total liabilities, surplus and other funds			<u>\$ 11,173,867</u>	

Underwriting and Investment Exhibit  
for the Year Ended December 31, 2004

Statement of Income

Underwriting Income

Premiums earned		\$ 3,410,199
Deductions:		
Losses incurred	\$ 2,806,468	
Loss expenses incurred	832,666	
Other underwriting expenses incurred	<u>1,925,412</u>	
Total underwriting deductions		<u>5,564,546</u>
Net underwriting loss		(2,154,347)

Investment Income

Net investment income earned	\$ 253,567	
Net realized capital gains	<u>29,486</u>	
Net investment gain		<u>283,053</u>
Net loss before federal income taxes		<u>(1,871,294)</u>
Net loss		<u>\$ (1,871,294)</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2003		\$ 6,550,333
Net loss	\$ (1,871,294)	
Net unrealized capital losses	(304)	
Change in net deferred income tax	209,307	
Change in nonadmitted assets	(210,567)	
Surplus adjustments: Paid-in	<u>1,500,000</u>	
Change in surplus as regards policyholders for the year		<u>(372,554)</u>
Surplus as regards policyholders, December 31, 2004		<u>\$ 6,618,054</u>

Reconciliation of Surplus as Regards Policyholders  
from December 31, 2001 through December 31, 2004

Surplus as regards policyholders, December 31, 2001, per Examination	\$5,576,856
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	Gain in Surplus	Loss in Surplus
Net loss	\$	\$ 1,165,244
Net unrealized capital gains	304	
Change in deferred income taxes	45,886	
Change in nonadmitted assets		89,748
Surplus adjustments: Paid-in	2,250,000	
Totals	\$ 2,296,190	\$ 1,254,992
Net increase in surplus as regards policyholders		1,041,198
Surplus as regards policyholders, December 31, 2004, per Examination		\$ 6,618,054

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### (1) Cash and Short-Term Investments

The Company needs to establish a procedure to file its unclaimed property with the State Board of Equalization. It was noted that the Company has \$20,356 of unclaimed funds that should be escheated to the State.

### (2) Losses and Loss Adjustment Expenses

Loss and loss adjustment expense reserves were reviewed by a Casualty Actuary from the California Department of Insurance. Based on the review, it was determined that the reserves were reasonable as of December 31, 2004, and have been accepted for this examination.

## SUMMARY OF COMMENTS AND RECOMMENDATIONS

### Current Report of Examination

Management and Control - Management Agreements (Page 5): It is recommended that the Company execute an agreement with a qualified custodian and file the proposed agreement with the California Department of Insurance in advance as required by California Insurance Code Section (1104.9(c)). It is also recommended that the Company amend its management agreements to reflect the name change of the Company from Millennium Insurance Company to Alliance United Insurance Company.

Comments on Financial Statement Items - Cash and Short-term Investment (Page 11): The Company needs to establish a procedure to file its unclaimed properties with the State Board of Equalization.

### Previous Report of Examination

None

## ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and parent's employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

/S/

Sam Sohrab, CFE  
Examiner-In-Charge  
Senior Insurance Examiner  
Department of Insurance  
State of California